

CAMPEAU GOODSSELL SMITH
WILLIAM J. HEALY, ESQ. BAR NO. 146158
440 North First Street, Ste. 100
San Jose, California 95112
Telephone: 408.295.9555
Facsimile: 408.295.6606

Attorneys for Debtor

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In Re:

272 E Santa Clara Grocery, LLC

Debtor.

) Case No.: 13-53491

) **CHAPTER 11**

) **RESPONSE TO OBJECTION TO**
) **APPLICATION FOR ORDER**
) **APPOINTING COUNSEL FOR DEBTOR**

) **Date: August 21, 2013**

) **Time: 2:00 p.m.**

) **Place: United States Bankruptcy Court**
) **280 South First St., Rm 3099**
) **San Jose, CA**

) **Judge: Hon. Stephen Johnson**

COMES NOW, Campeau Goodsell Smith, L.C. ("CGS" or "Applicant) and submits the following reply to Boston Private Bank & Trust Company's ("BPB" and/or the "Bank") objection ("Objection") to Debtor's application ("Application") to employ CGS as Debtor's general bankruptcy counsel:

I. BPB's Objection to the Application is Limited and Misplaced.

BPB's Objection to the Application is limited to two claimed deficiencies of information,

RESPONSE TO OBJECTION TO APPLICATION FOR ORDER APPOINTING COUNSEL FOR DEBTOR

1 namely that the Application fails to fully disclose the “factual and legal relationships” between
2 the Debtor, the Andrew Lewis (“Mr. Lewis”) and CGS relative to the retainer and fails to
3 demonstrate the non-existence of facts that would “create non-disinterestedness, actual conflict,
4 or impermissible potential for conflict of interest”. The Objection is misplaced and should be
5 overruled.
6

7 **II. FACTUAL BACKGROUND.**

8 A brief background of the Debtor and the basis for the bankruptcy filing may help
9 demonstrate why the Objection is misplaced and should be overruled.
10

11 Debtor owns a single piece of real estate located at 272 E. Santa Clara, San Jose, CA
12 (“the Property). Debtor is owned by a several investors (collectively the “Investors”) and in
13 March 2012 the Investors formed the Debtor and deeded their respective ownership interests in
14 the Property to the Debtor. BPB is not a direct creditor of the Debtor, but holds a deed of trust on
15 the Property. Prior to the formation of the Debtor, the Investors held a deed of trust on the
16 Property junior to BPB and foreclosed. At the time of the foreclosure, the Property was empty—
17 no tenant and no income. Between October 2011 and March 2012, the Investors marketed the
18 Property for lease, found and secured a tenant, and paid \$242,000 in leasing commissions. At the
19 same time the Investors were paying BPB \$24,307.45 per month to keep its loan current.
20

21 In March 2012 Debtor entered into a 10-year lease of the Property with Grocery Outlet, Inc., a
22 national grocery store chain, wherein the tenant pays rent of \$39,600 per month (triple net).
23

24 Debtor is solvent with the current value of the Property at \$7.3 million, based on a pre-petition
25 contract to sell the Property, and total outstanding liabilities of approximately \$4.3 million.
26
27
28

1 In November 2012 the Debtor entered into a contract to sell the Property for \$7.3 million.
2 Escrow was scheduled to close in December 2012 and the sale would have paid off BPB's lien.
3 However, the buyer cancelled the sale after discovering that the Property was undergoing clean-
4 up or investigation due to a possible leak from an old underground storage tank. The buyer's
5 discovery was Debtor's first notice of any contamination on the Property. Debtor was informed
6 that BPB had been aware of the contamination since 2008, had a copy of a report showing
7 purported contamination, and never disclosed the report or the purported contamination to
8 Debtor.
9

10
11 Since December 2012 Debtor has been working to address the environmental issue,
12 secure governmental clearances, and sell the Property and pay BPB and all creditors in full.

13 Debtor filed for bankruptcy protection after BPB, contrary to its prior agreements with
14 Debtor and most recent verbal extension of that agreement demanded Debtor release all claims
15 Debtor had against BPB, began intercepting 100% of the rent (approximately \$39,000 and
16 \$15,000 more than BPB's monthly loan payment), and moved towards foreclosure. BPB's
17 interception of 100% of the rent has left Debtor without monthly income.
18

19 Debtor retained CGS to represent it as general bankruptcy counsel. CGS, in discussions
20 with the Debtor, agreed to a \$20,000 retainer. As BPB had intercepted 100% of Debtor's income,
21 Debtor was unable to immediately fund the retainer. Debtor's manager and member Andrew A.
22 Lewis ("Mr. Lewis") agreed, pre-petition, to loan to the Debtor of \$20,000.00 in order to fund
23 CGS's retainer. The Application and associated Attorney Client Fee Agreement do not suggest
24 that Mr. Lewis has agreed to be responsible for or pay all of CGS's legal fees and he has not so
25 agreed.
26
27
28

1 **III. LEGAL AUTHORITY**

2 **a. The Disinterested Issue Relating to Employment of Debtor's Counsel Is**
3 **Based on Disclosure and Concerns of a Misaligned Duty of Loyalty.**

4 CGS is disinterested, disclosed its relationship to the Debtor, and its duty of loyalty runs
5 to the Debtor. As CGS's only contractual relationship is with the Debtor, the Debtor's payment
6 of CGS's retainer comes from Debtor pursuant to a pre-petition loan to the Debtor by Mr. Lewis,
7 and such has been disclosed. Debtor's and Mr. Lewis's interests are aligned such that no duty of
8 loyalty concerns warrant the objection to CGS's employment.

9
10 While some courts raise concerns regarding counsel's duty of loyalty when legal fees are
11 paid by a third party/insider, not all take a uniform or per se approach in addressing this issue
12 and most focus on whether the parties interests are aligned. Some courts have announced a per se
13 rule stating that such arrangement violates 11 USC 327 unless the Debtor and the third
14 party/insider are aligned, others have rejected it. *In re Hathaway Ranch Partnership*, 116 B.R.
15 208 Bankr.C.D.Cal.1990); see also *In re Lotus Properties LP*, 200 BR 388, (Bankr. C.D.,
16 California 1996). Several prior bankruptcy court decisions from the Ninth Circuit are in accord
17 with *Hathaway* but involve serious allegations of misconduct by the third party, inadequate
18 disclosure by counsel of the source of the retainer, dual representation by proposed counsel of
19 the bankruptcy debtor and a principal/insider, the failure of counsel to provide full disclosure of
20 all pertinent connections, and the presence of a reimbursement or guarantee arrangement. *In re*
21 *Lotus Properties LP*, 200 BR 388, 392 (Bankr. C.D, California 1996). Other Courts in our
22 district have rejected the pre se approach, especially when there is no indication of wrongdoing.
23 The basis for such rejection is that "many small corporations facing the threshold of the
24 Bankruptcy Court depend upon their key, and many times solvent, insiders to fund the debtor's
25
26
27
28

1 bankruptcy attorney for the latter's undertaking of vital pre-and post-bankruptcy representation".
2 *Id. at*, 393

3 Instead of a per se rule these courts look at the facts of the case to determine whether
4 counsel holds or represents an interest adverse to the estate, and is not disinterested. Courts have
5 used different tests to determine if counsel has a conflict. Some courts have used the Kelton's
6 guidelines promulgated by BPB's counsel while others courts have set different specific
7 guidelines. The *Missouri Mining* case had the following guidelines:
8

- 9
- 10 • whether there was any specific advantage to the third party;
 - 11 • whether there was any injury to the estate;
 - 12 • whether there was prejudice to other creditors; and
 - 13 • whether an actual conflict arising from the payment is apparent.
- 14

15 *In re Missouri Mining, Inc.*, 186 BR 946, 949 (Bankr.WD Missouri 1995) approved by *In*
16 *re Lotus Properties, LP*, 200 B.R. 388, 394 (stated Missouri Mining guidelines were similar to
17 the Kelton guidelines).

18 **b. The Interests of All Parties are Aligned and CGS Is Disinterested.**

19 The interests of all parties, including the Debtor, BPB, Mr. Lewis¹, and creditors, are
20 aligned-secure government clearance of the environmental issues, sell the Property, and pay all
21 creditors. However, because BPB has intercepted and continues to intercept 100% of Debtor's
22 income, BPB has prevented the Debtor from paying its obligations, including counsel, absent the
23 pre-petition loan from Mr. Lewis. There is not an actual or apparent conflict between the Debtor
24

25

26 ¹ Mr. Lewis, owns a 27% interest in the Debtor--Statement of Financial
27 Affairs (Doc#1).

1 and CGS and/or Mr. Lewis because the Attorney Client Fee Contract does not require Mr. Lewis
2 to pay CGS's fees.

3 The Debtor has complied with both the Missouri Guidelines and the Kelton Guidelines.
4
5 First, the Debtor has fully disclosed the debtor/client relationship as demonstrated by the
6 Application. Second, the Debtor gave its express consent to the fee arrangement by executing a
7 written fee agreement which fully disclosed the terms of that arrangement. Mr. Lewis has been
8 informed by CGS that the duty of loyalty is to the Debtor and not to Mr. Lewis and the fee
9 agreement is specifically between the Debtor and CGS. There is no specific advantage to Mr.
10 Lewis to agreeing to a pre-petition loan to the Debtor to pay CGS's retainer, there is no injury to
11 the estate, the arrangement does not prejudice the other creditors, and there is no actual conflict.
12 In fact, Debtor and creditors benefit from Mr. Lewis' pre-petition loan as it enabled Debtor to
13 secured counsel and file this bankruptcy. CGS's compensation is subject to court approval and
14 any compensation beyond the retainer it to come from the Debtor and not Mr. Lewis.
15
16

17 **IV. Conclusion.**

18 Based on the foregoing, Debtor requests that CGS be employed as general bankruptcy
19 Counsel and BPB's objection be overruled.
20

21 Dated: August 9, 2013

CAMPEAU GOODSSELL SMITH

22 By: /s/: William J. Healy
23 William J. Healy
24 Attorneys for the Debtor
25
26
27
28